



**DEPARTMENT OF THE TREASURY**

**INTERNAL REVENUE SERVICE**

**1100 Commerce Street**

**MS:4920:DAL, Attn: Mandatory Review**

**Dallas, TX 75242**

**TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION**

**Date: June 19, 2008**

**Number: 200837042**

**Release Date: 9/12/2008**

**LEGEND**

ORG = Organization name

XX = Date

Address = address

UIL:501.07-01

**ORG**

**ADDRESS**

**Employer Identification Number:**

**Person to Contact/ID Number:**

**Contact Numbers:**

**Voice:**

**Fax:**

**CERTIFIED MAIL – RETURN RECEIPT REQUESTED**

**Dear :**

In a determination letter dated April 19XX, you were held to be exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code (the Code).

We have determined you have not operated in accordance with the provisions of section 501(c)(7) of the Code. Accordingly, your exemption from Federal income tax is revoked effective January 1, 20XX. This is a final adverse determination letter with regard to your exempt status under section 501(c)(7) of the Code.

We previously provided you a report of examination explaining why we believe revocation of your exempt status is necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On February 2, 20XX, you signed Form 6018-A, *Consent to Proposed Action*, agreeing to the revocation of your exempt status under section 501(c)(7) of the Code.

You are therefore required to file Form 1120-H, U.S. Income Tax Return for Homeowners Association, for the year[s] ended December 31, 20XX, and December 31, 20XX with the Ogden Service Center. You have submitted Form 1120-H and paid the tax for tax years ending December 31, 20XX, and

December 31, 20XX. In addition, you submitted Form 1120-H and paid the tax

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for tax year ending December 31, 20XX. Forms 1120-H and the respective payments for tax years ending December 31, 20 , December 31, 20XX, and December 31, 20XX were submitted to the Ogden Service Center for processing. For future periods, you are required to file Form 1120-H with the appropriate service center indicated in the instructions for the return.

You have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,

Marsha A. Ramirez  
Director, EO Examinations



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

**DEPARTMENT OF THE TREASURY**

Internal Revenue Service  
TE/GE EO Examination  
1100 Commerce Street  
Dallas, Texas 75242

November 26, 2007

ORG  
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

**CERTIFIED MAIL – RETURN RECEIPT REQUESTED**

Dear :

We have enclosed a copy of our report of examination explaining why we believe an adjustment of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018, *Consent to Proposed Adverse Action*. We will then send you a final letter modifying or revoking exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become final. In that event, you will be required to file Federal income tax returns for the tax period(s) shown above. File these returns with the Ogden Service Center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Marsha A. Ramirez  
Director, EO Examinations

Enclosures:  
Publication 892  
Publication 3498  
Form 6018  
Report of Examination  
Envelope

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
<b>Name of Taxpayer</b>  ORG		<b>Year/Period Ended</b>  20XX12

**LEGEND**

ORG = Organization name      XX = Date      motto = motto

**Issue:**

Does the ORG continue to qualify for tax exemption status under Internal Revenue Code section 501(c)(7)?

**Facts:**

The ORG (ORG) was incorporated May 25, 19XX in the State of XYZ. The ORG's Articles of Incorporation identify their purpose and objects for which it is formed as:

- To foster the motto,
- To provide needed facilities for the benefit of its members,
- To cement the fellowship of the motto,
- To cooperate with all other ORGs similar in nature in the furtherance of the motto and,
- To carry out the foregoing purpose the corporation shall have power to receive and convey real and personal property and to lease and sublease property

The By-laws include the ORG's rules regarding what Members can or cannot do while living there. Membership rules include animal restrictions, parking restrictions, utility information, and permission for use of Clubhouse or Pavilion.

The gated property, which the ORG operates on, was purchased April 10, 19XX from the United States of America, acting by and through the District Engineer,      Corps of Engineers. Terms of the purchase agreement indicate the property shall be used for cottage site purposes only, and in the event of use for any other purposes, title to the land and improvements shall revert to and vest in the United States. The term "cottage site purpose" is defined to mean a colony site. The cottage site size is not to exceed one (1) acre and only one (1) dwelling shall be placed on any lot. The ORG retains ownership of land which has been divided into lots for member convenience to build member owned structures on the lots.

The ORG has three (3) types of Members including the following:

1. Regular Member - Only individuals or married couples
2. Dual Member - Adult children, mothers, and fathers of Regular Members who share their dwellings
3. Non-property Members - Regular Members who, by reason of sale, transfer of ownership, or otherwise, no longer own improvements

To acquire membership in the ORG a prospective member must approved by the Board of Directors. If approved by the Board; a prospective member must pay an initiation fee of \$ including sales tax; monthly dues of \$ for available lots. A prospective member can obtain a lot

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either through available vacancies or through the purchase of "improvements" on a lot from a Resigning Member of the ORG. New members acquiring property from a Resigning Member must separately from the ORG negotiate the purchase price of the improvement on the lots with that Resigning Member. Improvement can consist of any dwelling structures, wet/dry boat house, garages, carports or storages sheds.

Membership can be transferred in the same family. An agreement must be reached among all involved, and after notice to the ORG and approval by the Board of Directors, Regular Members and Dual Members in the same family may exchange respective member status.

A member may resign from the ORG at any time upon written notice to the ORG. Resignation will not relieve the Member from liability for unpaid dues or bills. Membership dues will continue to be payable until ownership of the improvements owned by the Resigning Member have been transferred to another Member, who assumes responsibility for dues, and all personal property of the Resigning Member has been removed from the ORG Premises.

The ORG provides member services such as water distribution lines to Member owned dwellings and trash removal services. Also, the ORG provides maintenance and improvements to the common areas on the property including a Clubhouse, pavilion, boat slips, boat ramp, fishing dock, swimming dock, basketball court, park, dry storage, and several open areas. The roadways around Member owned dwellings which are not part of the ORGs social facilities, areas around dry storage building, and walkways to boat house are kept clean and mowed by the ORG using member dues and assessments.

For the tax year ended December 31, 20XX, the ORG conducted several organized events. On May 14, 20XX the ORG held a Garage sale and Chili dinner where funds were raised from a raffle. The ORG also holds its annual Safety town hall meeting; Labor Day and Thanksgiving dinner was held for all members.

### **Law:**

Section 501(c)(7) of the Code provides for the exemption from Federal income tax of ORGs organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.

Section 1.501(c)(7)-1(a) of the Regulations states that the exemption provided by section 501(a) of the Code for an organization described in section 501(c)(7) of the Code applies only to ORGs which are organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, but does not apply to any ORG if any part of its net earnings inure to the benefit of any private shareholder. In general, this exemption extends to social and recreation ORGs which are

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supported solely by membership fees, dues and assessments. However, a ORG otherwise entitled to exemption will not be disqualified because it raises revenue from members through the use of ORG facilities or in connection with ORG activities.

Revenue Ruling 68-168, 1968-1 CB 269-A nonprofit organization that leases building lots to its members on a long-term basis is not exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code of 1954.

Revenue Ruling 75-494, 1975-2 CB 214-A ORG providing social and recreational facilities, whose membership is limited to homeowners of a housing development, will be precluded from qualifying for exemption under section 501(c)(7) of the Code by owning and maintaining residential streets, enforcing restrictive covenants, or providing residential fire and police protection and trash collection service.

Revenue Ruling 58-589, 1958-2 CB 266 sets forth the criteria or tests for determining whether an organization qualifies for exemption from Federal income tax under section 501(a) of the Internal Revenue Code of 1954 as an organization described in section 501(c)(7) of the Code. The ruling states that an organization must establish that it is a ORG both organized and operated exclusively for pleasure, recreation, and other non-profitable purposes and that no part of its net earnings inure to the benefit of any private shareholder or individual. To meet the first requirement, there must be an established membership of individuals, personal contacts, and fellowship. A commingling of the members must play a material part in the life of the organization. In addition, the ruling states that a ORG which engages in business, such as making its social and recreational facilities available to the general public or by selling real estate, etc. may not be considered as being organized and operated exclusively for pleasure, recreation, or social purposes.

In *Chattanooga Automobile ORG v. Commissioner*, 182 F. 2d 551 (6<sup>th</sup> Cir. 1950), the United States Court of Appeals 6<sup>th</sup> Circuit held that to be exempt under the Act of Congress, a ORG must have been organized and operated exclusively for pleasure, recreation, and other non-profitable purposes. The court further specified that the words "other non-profitable purposes" must be construed as coming within the same classification as pleasure and recreation. In addition, there must be at least some sort of commingling of members to constitute a ORG. The court held that the two automobile ORGs petitioning the court were not exempt under section 101(9) of the Internal Revenue Code of 1939 as a social ORG because the members of these ORGs did not commingle.

In *Keystone Automobile ORG v. Commissioner*, 181 F. 2d 402 (3<sup>rd</sup> Cir. 1950), the United States Court of Appeals 3<sup>rd</sup> Circuit defined the word "ORG" to include some type of mingling of people together as well as a common object. In this case, the court held that the Keystone Automobile ORG was not exempt under section 101 paragraph 9 of the Code for a number of reasons one of which was because they saw no evidence of the commingling of members.



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### **Government's Position:**

An organization, whose purpose is to provide facilities for the benefit of its members where fellowship among members is incidental, is not a social ORG. A social ORG must be organized for pleasure or recreational purpose in order to qualify for tax-exempt status under IRC section 501(c)(7). The Treasury Regulations extend tax-exempt status to those ORGs, organized for recreational purposes, which are supported by membership dues and assessments.

The ORG has not shown that its members are bound together by a common objective, and their activities do not demonstrate the sharing of active interest among members, and sharing of goals by members justifying the existence of the ORG.

Although fellowship need not be present between each member of the ORG, it must constitute a material part of the organization's activities. The absence of meaningful face-to-face interaction illustrates member contact is incidental to the primary purpose of the ORG. The lack of commingling indicates a basic purpose of providing personal services and goods to the membership in a manner similar to commercial counterparts.

Like the organization in *Keystone Automobile ORG v. Commissioner*, ORG has provided no evidence of meaningful commingling of members. Similar to, Rev. Rule 58-589, ORG has not shown there was an established membership of individuals, personal contacts, and fellowship among members.

Like Rev. Rule 68-168, ORG leases building lots to its member on a long-term basis. ORG acquired land and, after developing recreational facilities the remaining land was subdivided into lots for its lessee-members. Members' pay an amount based on the fair market value of the lot's improvements, then pays the ORG a one time membership fee of \$        and thereafter pays a nominal annual rental fee (dues). The subdividing and leasing of lots in the manner described constitutes engaging in business. Although the revenues from this activity are derived from the ORGs members only, the revenue are not raised from the members' use of recreational facilities, or in connection with the ORG's recreational activities. The conduct of such real estate activity, whether with members only or with the general public, is not incidental to or in furtherance of any purpose covered by section 501(c)(7) of the Code. Accordingly, the organization does not qualify for exemption from Federal income tax under that section.

Similar to the organization described in Rev Rule 75-494, ORG owns and maintains residential streets which are not part of its recreational facilities. Streets providing immediate access to a ORG's facilities could be considered part of the facility, and thus part of a social facility. However, most of the ORG's streets primarily serve residential areas which are not a part of a ORG's social facilities, even though members must travel on them to reach the ORG's recreational facilities. Thus, a ORG which owns and maintains residential streets is not operated

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exclusively for pleasure, recreation, and other non-profitable purposes. Also ORG provides trash removal and water distribution services to member-owned dwellings. A ORG may provide these services in connection with the maintenance of its recreational facilities. However, your services go beyond merely maintaining recreational facilities and include services to members at their dwellings, which are no longer exclusively in furtherance of pleasure and recreation. Thus, a ORG providing trash collection service and water distribution services to members will not qualify for exemption under section 501(c)(7) of the Code.

### **Taxpayer's Position**

Unknown

### **Conclusion**

As a result of our examination of your Form 990 for the period ended December 31, 20XX, we have determined that your organization no longer qualifies as an exempt social ORG described in IRC section 501(c)(7). We are proposing that the Corporation's exempt status be revoked as of January 1, 20XX. Form 1120, (U.S. Corporation Income Tax Return), should be filed for the fiscal years ended December 31, 20XX, 20XX and all future years.